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IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF ARIZONA

Lexington Insurance Company, a Delaware
Corporation,

Plaintiff,

v.

Scott Homes Multifamily, Inc., an Arizona
corporation; and Silverbell 290 Limited
Partnership, an Arizona Limited
Partnership,

Defendants.

No. CV-12-02119-PHX-JAT

ORDER

Pending before the Court are: (1) Plaintiff's Motion to Dismiss Silverbell 290 Limited Partnership's Counterclaim (Doc. 27) and (2) Scott Homes Multifamily, Inc.'s Motion to Dismiss (Doc. 41). The Court now rules on the Motions.

I. Background

A. The Complaint

On October 8, 2012, Lexington filed its Complaint in this Court. (Doc. 1) In its Complaint, Lexington alleges as follows:

On March 2, 2010, Defendant Silverbell 290 Limited Partnership ("Silverbell")¹

¹ Silverbell is a general partner of Timberline Village Corporation ("Timberline"). (*Id.* at ¶ 7). Timberline is owned by the Steven S. Robson Trust dated June 25, 1993 (the "Robson Trust"). (*Id.* at ¶ 8). Steven S. Robson is the trustee of the Robson Trust. (*Id.*)

1 sued Defendant Scott Homes Multifamily, Inc. (“Scott”), among others, in Pima County
2 Superior Court (the “state court case”). (*Id.* at ¶ 13). Silverbell is the owner of an
3 apartment complex called the Springs at Silverbell Apartments (the “Silverbell
4 Apartments”). (*Id.* at ¶ 6). In its Amended Complaint in the state court case, Silverbell
5 alleged that Scott was the general contractor in the construction of the Silverbell
6 Apartments pursuant to a contract, and that Scott, as general contractor, entered into
7 contracts, agreements, and/or subcontracts with subcontractors and/or others to assist in
8 the construction. (*Id.* at ¶¶ 16-17). In that Amended Complaint, Silverbell alleged that,
9 in late 2008, it discovered a number of defects and latent defects at the Silverbell
10 Apartments and that the damages exceed \$7.11 million. (*Id.* at ¶¶ 18-20).

11 Scott then tendered its defense and indemnity to Evanston Insurance Company
12 (“Evanston”) subject to a reservation of rights under Evanston CGL Policy No. 01 GLP
13 1003112 (the “Evanston Policy”). (*Id.* at ¶ 23).

14 Lexington issued an Excess Liability Policy No. 4013724, effective January 1,
15 2002 to January 1, 2003, to Robson Communities, Inc. (“Robson”) (the “Excess Policy”).
16 (*Id.* at ¶ 2). Scott is a named insured in that policy. (*Id.* at ¶ 4). The Evanston Policy is
17 the “underlying policy” to the Excess Policy. (*Id.* at ¶ 43).

18 On July 2, 2012, Robson and Scott provided notice to Lexington that Scott was
19 finalizing a settlement with Silverbell that would result in the exhaustion of the Evanston
20 Policy and would trigger coverage under the Excess Policy issued by Lexington. (*Id.* at ¶
21 24). On July 13, 2012, Lexington requested information from Robson and Scott
22 confirming the exhaustion of the Evanston Policy and any other underlying policies. (*Id.*
23 at ¶ 25). Thereafter, on July 20, 2012, Lexington again requested information confirming
24 the exhaustion of underlying policies and requested confirmation that the subcontractors’
25 policies had also been exhausted. (*Id.* at ¶¶ 26-27). On July 26, 2012, Lexington again
26 requested information concerning the subcontractors’ policies and positions taken by
27

28 The Robson Trust owns Scott Homes Multifamily, Inc. (*Id.* at ¶ 9). Steven S. Robson is
the president, secretary, and director of Scott Homes Multifamily, Inc. (*Id.* at ¶10).

1 their respective carriers. (*Id.* at ¶ 28). Lexington never received a response to these
2 requests. (*Id.* at ¶ 29).

3 On September 19, 2012, Silverbell, Scott, and Evanston agreed to enter into a
4 settlement agreement purporting to resolve the claims asserted against Scott in the state
5 court case for damages arising out of the project, including repair and replacement of
6 defective construction and resulting damages (the “Settlement Agreement”). (*Id.* at ¶¶ 30-
7 31). In that Settlement Agreement, Evanston agreed to pay Silverbell one million dollars,
8 the aggregate limit of its insurance under the Evanston Policy. (*Id.* at ¶ 32). The
9 Settlement Agreement further provided that the one million dollar payment exhausted
10 Evanston’s applicable coverage.

11 Further, Scott and Silverbell agreed to enter into a stipulated judgment against
12 Scott in the amount of six million dollars to be received from subcontractors,
13 subcontractor’s insurers, and Scotts’ primary and excess insurers (the “stipulated
14 judgment”). (*Id.* at ¶ 34). In Exhibit 1 to the Settlement Agreement, Scott identified
15 eleven subcontractors who unconditionally agreed to defend and indemnify Scott and
16 failed to do so. (*Id.* at ¶ 36). The Excess Policy applies only upon exhaustion of all
17 applicable underlying limits, whether or not collectible. (*Id.* at ¶¶ 46, 67).

18 As a result of the above allegations, Lexington seeks the following declarations:
19 (1) that the Excess Policy is not currently implicated and Lexington owes no duty to
20 defend Scott Homes (*Id.* at ¶ 74); (2) that it owes no coverage for any amount of the
21 stipulated judgment or any damages sought in the state court case because the damages
22 sought in the state court case are not a result of “property damage” as defined in the
23 Excess Policy (*Id.* at ¶ 81); (3) that it is not liable for property damages that did not occur
24 during the effective dates of the Excess Policy (*Id.* at ¶ 88); (4) that it owes no coverage
25 for any amount of the stipulated judgment or other damages sought not caused by an
26 “occurrence” (*Id.* at ¶ 92); (5) that it owes no coverage for any “property damage
27 exclusions” (*Id.* at ¶ 100); (6) that it owes no coverage for damages excluded by
28 “professional liability exclusions” (*Id.* at ¶ 107); (7) that it owes no damages that were

1 first incurred prior to the inception of the Evanston or Excess Policies (*Id.* at ¶ 116); (8)
2 that it owes no coverage under a policy in effect prior to January 1, 2002 (*Id.* at ¶ 121);
3 (9) that it owes no coverage for damages as a result of clean up, remediation, abatement,
4 or removal of mold, fungus, or yeast (*Id.* at ¶ 126); (10) that it owes no coverage for
5 damages attributable to breach of contract, breach of a third party beneficiary contract
6 and breach of implied and express warranties causes of action (*Id.* at ¶ 132); (11) that it
7 owes no coverage for damages attributable to “property damages” for the acts of
8 independent contractors that did not procure the requisite insurance (*Id.* at ¶ 137); (12)
9 that, to the extent Silverbell qualifies as an insured under the Excess Policy, no coverage
10 is available for any damages sought in the state court case (*Id.* at ¶ 145); (13) that, as a
11 result of Scott’s material breach of duty to cooperate with Lexington, no coverage is
12 available under the Excess Policy (*Id.* at ¶ 153); (14) that, as a result of Scott’s failure to
13 obtain Lexington’s consent before entering into a settlement agreement, no coverage is
14 available under the Excess Policy (*Id.* at ¶ 158); (15) that, as a result of Scott’s failure to
15 obtain permission to transfer its rights under the Excess Policy, no coverage is available
16 under the Excess Policy (*Id.* at ¶ 165); and (16) that, to the extent that stipulated judgment
17 is a product of collusion or is unreasonable, no coverage is available under the Excess
18 Policy (*Id.* at ¶ 173).

19 **B. The Counterclaim**

20 In response to the Complaint, Defendant Silverbell filed an answer and
21 counterclaim. In its Counterclaim, Silverbell alleges:

22 In November 2011, Lexington was informed of the possible excess liability
23 exposure as a result of the state court case. (Doc. 10 at ¶ 8). In March 2012, Silverbell
24 wrote to Lexington to provide Lexington with notice of Silverbell’s claim in the state
25 court lawsuit and offered to provide any information to Lexington regarding the claim
26 and the opportunity to appear and participate in a mediation between the parties (*Id.* at ¶
27 21). In July 2012, Robson and Scott wrote a letter to Lexington informing it of the
28 intention of Scott to enter into the settlement agreement, including an assignment of

1 Scott's rights under the Excess Policy to Silverbell, and requesting Lexington's coverage
 2 position. (*Id.* at ¶ 22). Scott provided Lexington with responses to its requests for
 3 information. (*Id.* at ¶ 23). Lexington ignored its insured's liability resulting in the
 4 assignment of Scott's rights under the Excess Policy and the settlement agreement. (*Id.*).
 5 When Lexington did not respond, Scott, in an effort to avoid a trial set for September 24,
 6 2012, which could have resulted in a damage award in excess of \$11,000,000, entered
 7 into the settlement agreement on September 19, 2012 and assigned its rights under the
 8 Excess Policy to Silverbell. (*Id.* at ¶ 24). Scott was not informed of Lexington's refusal
 9 to provide coverage until October 5, 2012. (*Id.* at ¶ 28). The Evanston Policy was
 10 exhausted, which triggered Lexington's obligations under the Excess Policy. (*Id.* at ¶¶
 11 30-31, 44, 49).

12 As a result of these allegations, Silverbell asserts that Lexington (1) breached its
 13 duty to defend, provide coverage, or indemnify Scott, which resulted in a breach of
 14 contract, and (2) breached its duty of good faith and fair dealing/insurance bad faith by
 15 refusing to provide a timely defense and/or coverage position.

16 **II. Plaintiff's Motion to Dismiss Silverbell's Counterclaim (Doc. 27)**

17 Lexington argues that Silverbell's breach of contract claim should be dismissed
 18 because Silverbell has failed to allege exhaustion of all applicable underlying limits.
 19 Lexington argues that, because of the failure to allege exhaustion of applicable
 20 underlying limits, Lexington could not have breached its duty to defend or to indemnify
 21 Scott and, thus, Silverbell has failed to state a claim upon which relief can be granted.

22 Lexington also argues that Silverbell's insurance bad faith/breach of the duty of
 23 good faith and fair dealing claim should be dismissed because Silverbell did not allege
 24 that Lexington acted unreasonably and intentionally.

25 **A. Legal Standard**

26 To survive a Rule 12(b)(6) motion for failure to state a claim, a counterclaim must
 27 meet the requirements of Rule 8. Rule 8(a)(2) requires a "short and plain statement of the
 28 claim showing that the pleader is entitled to relief," so that the counter-defendant has

1 “fair notice of what the . . . claim is and the grounds upon which it rests.” *Bell Atl. Corp.*
2 *v. Twombly*, 550 U.S. 544, 555 (2007) (quoting *Conley v. Gibson*, 355 U.S. 41 (1957)).

3 A counterclaim must contain sufficient factual matter, which, if accepted as true,
4 states a claim to relief that is “plausible on its face.” *Id.* Facial plausibility exists if the
5 pleader pleads factual content that allows the court to draw the reasonable inference that
6 the defendant is liable for the misconduct alleged. *Id.* Plausibility does not equal
7 “probability,” but plausibility requires more than a sheer possibility that a defendant has
8 acted unlawfully. *Id.*

9 In deciding a motion to dismiss under Rule 12(b)(6), the Court must construe the
10 facts alleged in a counterclaim in the light most favorable to the drafter of the
11 counterclaim, and the Court must accept all well-pleaded factual allegations as true.
12 *Shwarz v. United States*, 234 F.3d 428, 435 (9th Cir. 2000).

13 **B. Analysis**

14 With regard to its breach of contract claim, counterclaimant Silverbell alleges that
15 Scott informed Lexington of its intent to enter into a settlement agreement that would
16 trigger Lexington’s obligations under the Excess Policy due to exhaustion of the
17 Evanston Policy. Silverbell alleges that, despite numerous notices from Scott, Lexington
18 ignored its obligations to Scott under the policy causing Scott to enter into a Settlement
19 Agreement, assigning its rights to Silverbell to avoid a trial that would result in potential
20 liability of \$11,000,000.

21 Lexington argues that the Court should find that, based on the language of the
22 contract requiring the exhaustion of underlying insurance, Lexington’s obligations to
23 Scott under the Excess Policy were not triggered, and, thus, Silverbell cannot state a
24 claim for breach of contract. Silverbell argues that the language of the contract only
25 requires exhaustion of the Evanston Policy, which it alleges had been exhausted.

26 While the Parties dispute the meaning of the language in the Excess Policy
27 requiring Scott to exhaust underlying insurance, the Court need not address the scope of
28 the exhaustion requirement in the Excess Policy at this time because, even if the Court

1 were to agree with Lexington's interpretation of the Policy, the breach of contract
2 counterclaim could not be dismissed at this stage of the proceedings.

3 To determine whether the underlying insurance triggering the Excess Policy was
4 indeed insurance that needed to be exhausted as applied to the state court case and
5 whether such insurance was indeed exhausted, the Court would necessarily have to
6 consider evidence and facts outside of the scope of the allegations in the counterclaim,
7 which the Court is not permitted to do at the motion to dismiss stage. Although
8 Lexington argues that Silverbell's failure to allege that all policies insuring Scott were
9 exhausted is fatal to its claim, Silverbell has not alleged the existence of other policies
10 that would apply to the state court claims. Rather, Silverbell has alleged that the
11 applicable underlying insurance, namely the Evanston Policy, was exhausted. For the
12 Court to find that there are other policies that required such exhaustion, the Court would
13 necessarily have to consider evidence and/or counterdefendant's version of the facts,
14 which is not appropriate at the motion to dismiss stage. Accordingly, taking the facts
15 alleged in Silverbell's Counterclaim in the light most favorable to Silverbell, Silverbell
16 has stated a claim upon which relief can be granted in its breach of contract claim and the
17 motion to dismiss that claim is denied.²

18 Further, with regard to its claim for breach of the covenant of good faith and fair
19 dealing/insurance bad faith, Silverbell alleges that Scott informed Lexington on

20 ² Further, Lexington challenges most of Silverbell's factual allegations as
21 "conclusory." *See, e.g.*, Doc. 35 at 5 (arguing that Silverbell's allegation that the
22 Evanston Policy has been exhausted is conclusory and that the claim should be dismissed
23 because Silverbell "does not (and cannot) point to any facts that it has alleged in the
24 Counterclaim, which refute Lexington's argument that the policy issued by Evanston was
25 not exhausted.") (emphasis in original). At this stage, it is not Silverbell's burden to
26 refute Lexington's arguments. Rather, for the purposes of deciding the motion to dismiss
27 the counterclaim, the Court must accept Silverbell's allegations as true, whether or not
28 they can be proved. As such, the Court finds that these allegations are sufficiently
specific to put Lexington on notice of Silverbell's claims and the facts supporting those
claims. Further, the fact that Lexington offers controverting facts to challenge
counterclaimant's allegations does not make counterclaimant's allegations conclusory,
but rather contested. The Court will not resolve such contests at this stage of the
litigation.

1 numerous occasions that Scott believed the Excess Policy was triggered and requested
2 that Lexington provide it coverage or Lexington's position as to coverage. Silverbell
3 alleges that Scott responded to all of Lexington's requests for information, and that,
4 despite the fact that its duties were triggered, Lexington ignored Scott's requests for
5 coverage and refused to provide Lexington's position on coverage before the settlement
6 agreement was executed.

7 Lexington argues that the position it took with regard to the Excess Policy was
8 reasonable and thus cannot constitute the basis for a bad faith action. Again, the Court
9 cannot conclude that Lexington's position was reasonable without considering evidence
10 and facts outside the allegations in the counterclaim. Thus, construing Silverbell's
11 allegations in the light most favorable to Silverbell, Silverbell has stated a claim upon
12 which relief can be granted for breach of the covenant of good faith and fair
13 dealing/insurance bad faith and the motion to dismiss that claim is denied.

14 **III. Scott's Motion to Dismiss (Doc. 41)**

15 Defendant Scott argues that it should be dismissed because it assigned all of rights
16 in the Excess Policy to Defendant Silverbell. Defendant Scott further asserts that the fact
17 that Lexington has not stated a claim against Defendant Scott is demonstrated by
18 Lexington's admission in the Joint Case Management Plan that "no claims are being
19 asserted against Scott Homes in this lawsuit [and] Plaintiff only named Scott Homes as a
20 party because plaintiff believes Scott Homes' rights are directly affected by the outcome
21 of litigation." (Doc. 36 at 2 n. 1).

22 In Response, Lexington argues that it named Scott as a Defendant because it
23 believes that Scott is a necessary and indispensable party pursuant to Federal Rule of
24 Civil Procedure 19. Lexington also reiterates its argument that it has not stated a claim
25 against Scott, but that Scott's interests will be affected by the outcome of the litigation.

26 Determining whether a party is necessary under Rule 19 largely depends on
27 whether that party's interests will be "adversely affected [by the litigation] in a practical
28 sense." *Continental Ins. Co. of New York v. Cotton*, 427 F.2d 48, 51 (9th Cir. 1970).

1 In this case, although Lexington denies that it has stated a claim against Scott,
2 Lexington seeks declarations that it owes no coverage under the policy, in part, because
3 (1) Scott assigned its rights under the policy without Lexington's consent; (2) Scott
4 "materially breached its duty to cooperate with Lexington," which, Lexington alleges
5 would preclude coverage; and (3) the Stipulated Judgment entered into between Scott and
6 Silverbell was unreasonable and the result of collusion. The ultimate remedy that
7 Lexington seeks—to have the Court declare that no one is entitled to coverage under the
8 Excess Policy for the state court case—may not impact Scott because it assigned its
9 interest in the Excess Policy related to the state court case to Silverbell. However,
10 according to Lexington, for the Court to grant any such relief based on certain claims in
11 Lexington's complaint, the Court would have to make findings that Scott breached its
12 contract with Lexington and/or acted in collusion with Silverbell.³ If the Court were to
13 make such findings, there is no doubt that Scott's rights would be adversely affected by
14 the litigation in a practical sense.

15 Accordingly, based on the allegations in the Complaint, the Court finds that
16 Defendant Scott is a necessary party to this lawsuit and Scott's Motion to Dismiss is
17 denied.

18 **IV. Conclusion**

19 Based on the foregoing,

20 **IT IS ORDERED** that Plaintiff's Motion to Dismiss Silverbell 290 Limited
21 Partnership's Counterclaim (Doc. 27) is denied.

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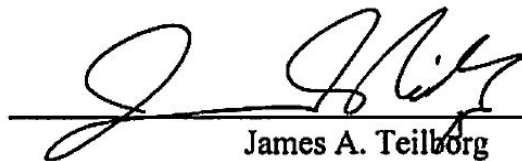
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27 ³ For the purposes of this Order, the Court takes no position as to whether
28 Lexington would actually be entitled to the remedy it seeks based on the allegations in
the Complaint.

1 **IT IS FURTHER ORDERED** that Scott Homes Multifamily, Inc.'s Motion to
2 Dismiss (Doc. 41) is denied.

3 Dated this 29th day of May, 2013.

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8 James A. Teilborg
9 Senior United States District Judge
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